



THE COMMITTEE ON ENERGY AND COMMERCE

INTERNAL MEMORANDUM

November 16, 2011

To: Members of the Subcommittee on Commerce, Manufacturing, and Trade

From: Majority Committee Staff

Re: Hearing on "Internet Gaming: Regulating in an Online World"

I. Summary

On Friday, November 18, 2011, the Subcommittee on Commerce, Manufacturing, and Trade will hold a hearing entitled "Internet Gaming: Regulating in an Online World" at 9:00 a.m. in room 2123 of the Rayburn House Office Building. Witnesses are by invitation only.

The purpose of this hearing is to continue the Committee's examination regarding the status of Internet gaming in the United States.

II. Witnesses

Panel I

The Honorable Frank Wolf
The Honorable John Campbell
The Honorable Barney Frank

Panel II

Mark Lipparelli
Chairman
Nevada Gaming Control Board

Charles McIntyre
Executive Director
New Hampshire Lottery Commission

Frank J. Fahrenkopf, Jr.
President and CEO
American Gaming Association

Dr. Rachel A. Volberg
Senior Research Scientist
NORC at the University of Chicago

III. Background

A. *Legal Status of Online Gaming*

Gaming policy and regulation is generally handled by the states, though the federal government has been involved in shaping the boundaries. By default, gambling is considered illegal unless expressly authorized by the state where it is conducted. With the exception of

Hawaii and Utah, all states have legalized some form of gambling (e.g., state lotteries, Bingo, Keno, card games, slot machines, casinos).

Forms of legal gaming authorized by states are: charitable gaming; lotteries; pari-mutuel gaming; Native American gaming; and commercial casino gaming. The total number of states which have authorized each of the various types of legal gaming are:

- A. Charitable gaming – 48 states
- B. Lotteries – 44 - (43 states + D.C.)
- C. Pari-mutuel gaming – 40 states
- D. Commercial casinos
 - a. Stand alone properties – 15 states (9 of these permit Indian casinos)
 - b. Racetrack casinos – 13
 - c. Indian casinos – 29 states

The legal status of online gaming is more complicated. In 1961, Congress passed the Interstate Wire Act.¹ According to the Justice Department, online gambling is illegal under the Wire Act because it prohibits the use of wire communications for the interstate facilitation or transfer of wagers.

In 1988, Congress passed the Indian Gaming Regulatory Act to address the jurisdiction and authority of tribes to establish gaming on their lands. The Act also established the National Indian Gaming Commission (NIGC) and its enumerated powers. Since passage of the Indian Gaming Regulatory Act, tribal gaming operations have seen tremendous growth. According to the NIGC, tribal gaming revenues in 2010 were \$26.5 billion derived from 422 gaming operations.

B. Unlawful Internet Gambling Enforcement Act (UIGEA)

In 2006, to combat the proliferation of unlawful Internet gaming, and consistent with the recommendations of the National Gambling Commission's 1999 report, Congress adopted the Unlawful Internet Gambling Enforcement Act (UIGEA).² The UIGEA effectively outlawed interstate online gaming in the United States by prohibiting gambling-related businesses from accepting payments in the form of checks, credit card payments, or electronic funds transfers (EFTs) relating to unlawful Internet gambling. The law also sets fines and penalties for banks and financial companies that process such payments.

Under implementing regulations that became effective in 2010, banks are required to conduct due diligence to "know their customer," have customer agreements barring illegal transactions, and have a remedial process to address illegal transactions when they are identified.

¹ P.L. 87-216.

² Title VIII of P. L.109-347, the SAFE Port Act.

Because the legality of the transaction is determined based on the underlying state or federal gambling law, some uncertainty and confusion have arisen.

Adding to the complexity and legal uncertainty, the law excludes *intrastate* transactions from the definition of “unlawful Internet gambling” so long as certain conditions are met, consistent with state law. Such a transaction must be made solely within a state, and the wager and method of placing the wager must be expressly authorized by that state. Additionally, the state law must provide for age and location verification; provide data security standards; and must not violate the Interstate Horseracing Act, the Professional and Amateur Sports Protection Act, the Gambling Devices Transportation Act, or the Indian Gaming Regulatory Act. Similarly, certain types of tribal gambling transactions are also excluded from the definition of “unlawful Internet gambling” under UIGEA, subject to stated conditions.

C. *State Developments in Online Gaming*

Although most states have taken no action regarding online gaming, several states have sought to expand or restrict the availability of intrastate online gaming. Seven states have enacted express prohibitions on internet gambling (Illinois, Indiana, Washington, Louisiana, Oregon, Montana, and South Dakota). The laws vary in their prohibitions, with some targeting businesses that only operate online, while at least one (state of Washington) also prohibits its citizens from gambling online.

Other states have interpreted the federal laws as permitting intrastate online gaming and have begun the process to authorize different forms of remote gaming. Nevada has already provided for remote intrastate sports wagering through mobile phone devices (Blackberry-enabled) in Nevada. State officials do not consider that application to be online gaming because it is viewed as another means of phone wagering, which is already legal in Nevada.

In any case, Nevada is forging ahead with online gaming. The state legislature passed a law in June 2011 legalizing “interactive gaming”. Although “interactive gaming” is defined broadly, Nevada’s gaming commission issued the first set of draft regulations in August (available at http://gaming.nv.gov/documents/pdf/reg5a_proposed_11aug11.pdf) that will only license online poker and prohibit businesses from accepting payments for any other type of wager.

The District of Columbia enacted the D.C. Lottery Modernization Act of 2010 to provide the D.C. lottery a framework to offer internet poker, bingo, and casino games to its residents. However, implementing regulations are still being developed.

Five states permit advance purchase subscription sales for lotteries they offer (New York, Virginia, Minnesota, North Dakota, and New Hampshire), and Illinois passed a law that allows a pilot program to sell lottery tickets through the internet though the program has not yet begun. Legislation has also been introduced in other states to facilitate online gaming, including two bills in California, though no action has been taken on either bill.

Efforts to repeal UIGEA, either in whole or in part, began in 2007. Proponents of repeal argue that the statute has not reduced Internet gambling but only driven it underground and offshore, where unscrupulous entities can operate with impunity. Legalizing Internet gambling,

they argue, would actually allow the government to provide greater protection for consumers than they have now. Regulation would address the many forms of fraud that take place in the Internet gambling world by requiring fair games and a dispute resolution process – recourse that consumers may not have with operations based in foreign jurisdictions. Some proponents also argue that if Internet gambling is legalized, the United States would realize significant tax revenues from online play that are currently directed to non-U.S. based gaming companies. The gaming industry estimates that Americans were wagering \$16 billion a year on Internet poker sites alone by 2010.³

Proponents of the ban argue that repealing the ban will expose more citizens to problems such as compulsive gambling, particularly in the segment of the population most susceptible to such habits: underage males. Additional concerns include a growth in fraud (both in outright financial fraud and with regard to the fairness of the games), money laundering, crime and terrorism financing, and the sharing or selling of player information. Others have expressed concern that state budgets could be harmed by the loss of lottery and gaming revenue and that some brick and mortar businesses could be disproportionately impacted by online gaming.

IV. Issues for Discussion

- How effective is current enforcement of online gaming in jurisdictions that have legalized it? How are states preparing to deal with the issue?
- What, if any, forms of interstate online gaming should Congress consider allowing?
- What consumer protections exist for online gaming?
- How would any easing of legal restrictions on Internet gaming affect consumers and other stakeholders?

Please contact Brian McCullough, Gib Mullan, or Shannon Weinberg at (202) 225-2927 with any questions.

³ See <http://www.nytimes.com/2011/10/09/technology/internet/in-online-poker-a-push-to-legalize-and-regulate-the-game.html?pagewanted=all>.